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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1960

No. _____

GROVER D. TURNBOW and RUTH H. TURNBOW,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
to the United States Court of Appeals
for the Ninth Circuit

Grover D. Turnbow and Ruth H. Turnbow pray that a writ of certiorari issue to review the judgment entered in this case on December 5, 1960, by the United States Court of Appeals for the Ninth Circuit, which reversed the judgment of the Tax Court of the United States entered August 31, 1959.

reorganization under § 112(g)(1)(B), gains on the exchange of the stock as well as to the extent of the cash received should be recognized. In so ruling it completely disregarded the specific direction in § 112(c)(1), providing that if the exchange would be within the provisions of § 112(b)(3)—i.e., would qualify as a reorganization—*if* it were not for the fact that the property received in the exchange consisted not only of stock but also of money,

> "then the gain * * to the recipient shall be recognized, but in an amount not in excess * * of such money * * *."

In so ruling the court also adopted an interpretation, directly contrary to that in the *Howard* case, of the provisions of § 112(e) of the 1939 Code (53 Stat. 39; Appx. A, infra, p. i), the correlative section dealing with *losses* from exchanges not solely in kind. *Howard* pointed out that the Commissioner's position would permit a taxpayer to escape the application of this provision by adding a nominal amount of cash to a stock-for-stock exchange and thus convert a paper loss into a tax loss. In the instant case, the court below considered that "Congress would seem to have weighed" these "undesirable potentialities" against the interpretation adopted by the court and to have accepted the consequences (R. 65).

REASONS FOR GRANTING THE WRIT

1. The decision below is directly in conflict with the decision of the Court of Appeals for the Seventh Circuit in Howard v. Commissioner of Internal Revenue (7 Cir. 1956) 238 F.2d 943.

The *Howard* case involved an exchange of stock for stock and cash. Some of the old shareholders received solely new stock for their old stock, others received solely cash for their old stock, and a few received both stock and cash for their old shares. After determining that the payment of the cash to some prevented the entire exchange from constituting a tax-free reorganization within the provisions of § 112(b)(3), the court then proceeded to determine whether the boot provisions of § 112(c)(1) applied to the exchange so as to postpone recognition of gain on the stock received. The court met and rejected the identical arguments which the Commissioner makes and the court below adopted in the instant case, and held that the presence of the cash payment, since *without* it the requirements of § 112(b)(3) would be met, did not defeat the application of § 112(c)(1) and no gain would be recognized except to the extent of the cash payment. The court said (pp. 947-948):

> "Petitioners [the taxpayers] contend that, in considering whether § 112(c) (1) applies to this transaction, it is necessary to look to § 112(b) (3) after omitting from consideration the cash payment involved in the transaction. On the other hand, respondent [the Commissioner] urges that there must be a qualifying reorganization within the meaning of § 112 (g) (1) (B) or (C) before § 112(c) (1) can come into play. He takes the position that 'section 112(c) makes it possible for other property or "boot" to be

received in the course of a reorganization without destroying qualification under the statute. This leeway does not, however, extend to the second and third types of reorganization namely reorganizations under section 112(g) (1) (B) and 112(g) (1) (C).'

We see no logical basis for this distinction. * * *

Thus we may conclude that, in determining when these so-called 'boot' provisions apply, Congress intended that the transaction is to be considered separate and apart from the 'boot' received in determining whether it meets the nonrecognition provisions. If the transaction, absent the 'other property or money', fulfills the requirements of § 112(b) (3), then gain is to be recognized to the extent that 'boot' is received.

In the present case, *but for* the cash received in exchange for 19.81% of the common stock of Binkley, the transaction would have met the 'solely' requirement of § 112(g) (1) (B) and fallen within the scope of § 112(b) (3). To the extent that 'boot' was received, gain would be recognized under our interpretation of the application of § 112(c) (1)" (italics by the court).

The decision below is also directly in conflict with the *Howard* decision on the important question of the tax treatment of *losses* from exchanges of property not solely in kind, under § 112(e) of the Internal Revenue Code of 1939. That statute, paralleling the language of § 112(c) (1), provides:

"If an exchange would be within the provisions of subsection (b)(1) to (5), inclusive, * * of this section if it were not for the fact that the property received in exchange consists not only of property permitted

> by such paragraph to be received without the recognition of gain or loss, but also of other property or money, then no loss from the exchange shall be recognized."

The parallel language of the two sections demands a like reading (*Davies Warehouse Co. v. Bowles* (1944) 321 U.S. 144, 150)—a proposition recognized both in *Howard* (238 F.2d 948) and by the court below (R. 64). In *Howard*, the Court of Appeals for the Seventh Circuit reviewed the legislative history of § 112(e), particularly the report of the House Ways and Means Committee (H.Rept. 179, 68th Cong., 1st Sess., p. 15; C.B. 1939-1, Pt. 2, pp. 241, 252) explaining the precursor of that statute (238 F.2d 948):

> "*Unless some provision is made for cases in which part of the consideration is money, the provisions of subdivision (b) could be avoided and the entire amount of the loss recognized if a small amount of money were received in addition to the specified property.* The only way to cover such a case and prevent the taxpayer from taking the entire loss by adding a small amount of money to the property received is to provide that no loss shall be recognized, otherwise the law might be evaded" (italics by the court).

From this the court concluded, as quoted supra, page 8, that Congress intended the transaction to be considered separate and apart from the "boot" received in determining whether it met the nonrecognition provisions—thus confirming its like conclusion as to the interpretation of § 112(c)(1). In the instant case the court below expressly referred to this determination in the *Howard* case (R. 64) and refused to follow it. Instead the court below assumed that Congress accepted the potentialities

of tax evasion (converting paper losses into tax losses by injecting a trifling amount of cash) which attend the Commissioner's argument (R. 65).

The *Howard* decision accords with every other decision of which we are aware, which involves the disregard of boot in testing the applicability of provisions for limited recognition of gain. These decisions include *First Seattle D. H. Nat. Bank* v. *Commissioner of Int. Rev.* (9 Cir. 1935) 77 F.2d 45, 47-49; *Elizabeth Bruce* (1934) 30 B.T.A. 80, 82-83; *Luther Bonham* (1936) 33 B.T.A. 1100, 1104 (relied on by the Tax Court in the instant case); and *R. C. Love* (1939) 39 B.T.A. 172, 180. In disputing *Howard,* the decision below disputes these other decisions also.

2. The decision below is erroneous:

a. The decision contravenes the plain and literal reading of the statute. The words as written are the expressed intent of Congress (*United States* v. *Mo. Pac. R. Co.* (1929) 278 U.S. 269, 278). As noted above, § 112(c)(1) plainly declares that:

> "If an exchange would be within the provisions of subsection (b) • • (3) • • of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph • • to be received without the recognition of gain, but also of • • money, then the gain • • to the recipient shall be recognized, but in an amount not in excess of • • such money • •."

And § 112(b)(3) provides:

> "No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganiza-

> tion are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization."

Here, "if it were not for the fact that" the property received in exchange consisted not only of voting stock of Foremost but also of money, the transaction would have been not only a stock-solely-for-stock exchange (§112(b)(3)), but also a reorganization as mentioned in § 112(b)(3) and as defined in § 112(g)(1)(B). Nothing in § 112(c)(1) warrants reading the "if it were not for the fact" clause as applying to the "solely for stock" postulate but not to the "reorganization" postulate. The literal reading of the words of Congress dictates the contrary.

In reasoning to its conclusion, the court below falls into several errors of statement. For example, the decision indicates as a necessary part of the taxpayer's and the Tax Court's position, that "(B)-type" reorganizations (i.e., reorganizations as defined in § 112(g)(1)(B), Appx. A, infra, p. ii) "can hypothetically exist notwithstanding boot" (R. 63). On the contrary, the taxpayer's and the Tax Court's position explicitly refers to transactions which *are not* "(B)-type" reorganizations because boot is present, but which *would be* (B)-type reorganizations if the boot were not present—and such is the transaction in the instant case. Similarly, the court's summation concluding that "§ 112(c) cannot operate to render a stock-plus-boot acquisition a (B) or (C) reorganization through a disregard of the existence of boot" (R. 66) reflects the same distortion; it has never been contended that the transaction *is* a (B)-type reorganization (whereupon there would

be *no* gain immediately recognized), but only that if the existence of boot is disregarded as § 112(c) hypothesizes, the transaction *would have been* a stock-solely-for-stock reorganization.

This non sequitur is the essence of the Commissioner's position. The argument comes down to this: the transaction as it stands is not a "reorganization" because of the money ingredient; therefore the transaction as it stands does not come within the total tax deferment of § 112(b)(3); therefore the transaction as it stands does not come within the partial tax deferment of § 112(c)(1) because of the money ingredient. This is a perversion of the plain language of § 112(c)(1).

b. The decision states a rule of construction which admittedly would necessarily apply to the identical language of § 112(e), the counterpart of § 112(c) dealing with losses. As shown above, such construction is contrary to the intent of Congress as expressly stated in the Committee report showing the reason for this provision—all as emphasized by the court in *Howard*, supra.

c. The decision contravenes the basic policy of the income tax structure, which is to tax immediately the gain from sales or exchanges of property to the extent of the receipt of money or property other than in kind, and to postpone taxation of the property received in kind until it should become the subject of some later taxable transaction. This is the manifest policy which runs throughout §§ 112(a), 112(b), 112(c) and 112(e).

The reorganization provisions are "tax-*deferring*, rather than tax-*exempting*, provisions" (Paul, Studies in Federal Taxation, Third Series, 1940, p. 4). They "are deemed

by Congress to be transitional, continuing transactions which are not sufficiently 'closed' to justify *economically* • • the imposition of capital gains tax at the immediate moment." As to other types of income in the form of the equivalent of cash, there is an immediate imposition of tax; but "the legislative intent in the reorganization provisions is to permit nothing more than a postponement of tax incidence to some future time when there is more than a 'mere change in the form of ownership'" (id. pp. 4-5).

This policy fits the instant case. The taxpayer has paid the tax on the cash component. On the voting stock component, Congress has postponed the imposition of the tax until the taxpayer sells or otherwise disposes of the stock in some way so as to convert any paper profit into an actual profit. When that time comes, Turnbow will be taxable on the gain eventually realized. There is no tax avoidance.

The Congressional committee reports express both policy and effect. Ushering in the original forerunner of § 112(c)(1), House Report 1432 of the 67th Congress, 4th Session (C.B. 1939-1, Pt. 2, p. 845),[4] after exemplifying the limited tax on a stock-for-stock-plus-cash exchange, stated:

> "The reason for this is that the profit, so far as it is contained in the new stock received, had not yet been realized, and therefore should not be taxed until the new stock is sold or in some way disposed of so that the profit will be actually realized."

---

[4]Approved by the Senate without change (S.Rept. 1113, 67th Cong., 4th Sess. (C.B. 1939-1, Pt. 2, p. 845)).

And when the 1939 Code was adopted, the House Committee thus explained its operation (H.Rept. 855, 76th Cong., 1st Sess., C.B. 1939-2, p. 518):

> "It has long been the policy in our income tax law to give due consideration to the exigencies of business in connection with corporate reorganizations by postponing, in certain specifically described instances, the recognition of gain realized in such transactions. In general, if gain is realized in such a transaction, nonrecognition of the *entire* gain is allowed only where under the specifically defined circumstances, the taxpayer transfers property and receives in exchange therefor *stock or securities in a corporation which is a party to the reorganization.* If, *in addition to such stock* [i.e., stock in a corporation which is a party to a reorganization] or securities, *other property or money is received,* gain is recognized to the extent of such other property or money" (emphasis added).

These are plain expressions of the intent of Congress. They confirm the literal language of the statute.

3. The decision below presents continuing questions of importance under present tax laws.

The provisions of §§ 356(a) and 356(c) of the Internal Revenue Code of 1954 (Appx. A, infra, p. iii), which correspond to §§ 112(c)(1) and 112(e) of the 1939 Code, contain substantially the same language and certainly the same pattern. The Commissioner's reiteration in the court below of his position which the Court of Appeals for the Seventh Circuit had rejected in the *Howard* case demonstrates that he will continue to oppose *Howard* and *Bonham* until this Court resolves the conflict. Uncertainties inherited from the decision below vis-á-vis the *Howard* and

Bonham decisions must attach to the 1954 Code provisions as well as to the 1939 Code. The ready means of converting a paper loss into a tax loss by injecting a nominal amount of cash, which would flow from the interpretation adopted by the court below, may seriously affect the national revenue if its decision is allowed to stand.

The uncertainties and conflicts outlined above may well affect a great number of taxpayers and transactions, both past and future. Such uncertainties will continue to exist until resolved by this Court. Clear understanding is essential both to the security of business transactions and to the administration of the revenue laws.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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(Appendices Follow.)

Appendix A

Internal Revenue Code of 1939:

"Sec. 112. *Recognition of gain or loss—*

(a) *General rule.* Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(b) *Exchanges solely in kind—*

• • • • • •

(3) *Stock for stock on reorganization.* No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

• • • • • •

(c) *Gain from exchanges not solely in kind.* (1) If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5), or within the provisions of subsection (1), of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph or by subsection (1) to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

• • • • • •

(e) *Loss from exchanges not solely in kind.* If an exchange would be within the provisions of subsection (b) (1) to (5), inclusive, or (10), or within the

provisions of subsection (l), of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain or loss, but also of other property or money, then no loss from the exchange shall be recognized.

• • • • •

(g) *Definition of reorganization.* As used in this section (other than subsection (b) (10) and subsection (l)) and in section 113 (other than subsection (a) (22))—

(1) The term 'reorganization' means (A) a statutory merger or consolidation, or (B) the acquisition by one corporation, in exchange solely for all or a part of its voting stock, of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation, or (C) the acquisition by one corporation, in exchange solely for all or a part of its voting stock, of substantially all the properties of another corporation, but in determining whether the exchange is solely for voting stock the assumption by the acquiring corporation of a liability of the other, or the fact that property acquired is subject to a liability, shall be disregarded, or (D) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its shareholders or both are in control of the corporation to which the assets are transferred, or (E) a recapitalization, or (F) a mere change in identity, form, or place of organization, however effected.

(2) The term 'a party to a reorganization' includes a corporation resulting from a reorganization

and includes both corporations in the case of a reorganization resulting from the acquisition by one corporation of stock or properties of another."

53 Stat. 37-40.

Internal Revenue Code of 1954:

"Sec. 356. *Receipt of additional consideration*

(a) *Gain on exchanges.*—

(1) *Recognition of gain.*—If—

(A) section 354 or 355 would apply to an exchange but for the fact that

(B) the property received in the exchange consists not only of property permitted by section 354 or 355 to be received without the recognition of gain but also of other property or money,

then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

• • • • •

(c) *Loss.*—If—

(1) section 354 would apply to an exchange, or section 355 would apply to an exchange or distribution, but for the fact that

(2) the property received in the exchange or distribution consists not only of property permitted by section 354 or 355 to be received without the recognition of gain or loss, but also of other property or money,

then no loss from the exchange or distribution shall be recognized."

68A Stat. 115-116.

Appendix B

[R. 29] In the Tax Court of the United States.

GROVER D. TURNBOW AND RUTH H. TURNBOW, PETITIONERS, *v.* COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

Docket No. 69429. Filed June 12, 1959.

Petitioner, who owned all of the stock of Supply, exchanged all of such stock for shares of stock of Foremost Dairies, Inc., and $3,000,000. He reported gain limited to $3,000,000, less expenses, under section 112(c)(1), 1939 Code. Respondent determined that gain in excess of $3,000,000 was taxable because section 112(c)(1) was not applicable. *Held,* the provisions of section 112(c)(1) are applicable and petitioner's gain is recognized but only in an amount which does not exceed the cash payment.

M. W. Dobrzensky, Esq., and *S. H. Dobrzensky, Esq.,* for the petitioners.

Nat. F. Richardson, Esq., for the respondent.

The Commissioner determined deficiencies in income tax for the taxable years 1952 and 1953 in the amounts of $264,037.43 and $14,786.26, respectively. The question is whether or not section 112(c)(1), 1939 Code, applies to a transaction in which petitioner received cash and stock in an acquiring corporation in exchange for all of the stock in another corporation, which became a subsidiary of [R. 30] the acquiring corporation, so that the taxable gain to be recognized is limited to the amount of cash received.

FINDINGS OF FACT.

The petitioners, residents of San Francisco, California, filed joint income tax returns for the taxable years with the collector of internal revenue for the first district of California. Since the issue to be decided relates only to Grover D. Turnbow, he is referred to hereinafter as the petitioner.

Petitioner owned all of the outstanding stock of International Dairy Supply Co. (a Nevada corporation) and International Dairy Engineering Co. (a California corporation). International Dairy Supply Co. (a Nevada corporation) owned 60 per cent of the stock of Diamond Dairy, Inc., and a group of individuals represented by petitioner owned the remaining 40 per cent of the stock of Diamond Dairy, Inc.

Foremost Dairies, Inc., a New York corporation (hereinafter called Foremost), which has its principal place of business in Jacksonville, Florida, is engaged in the business of processing and distributing milk, cream, and other dairy products.

International Dairy Supply Co. (hereinafter called Supply[1]) had, and still has, its principal office in San Francisco. The main part of its business was furnishing reconstituted milk and [R. 31] milk products to the Armed Forces of the United States, located outside the country, under contracts with the United States. Supply prepared dehydrated milk and milk products in this country and shipped such products to plants, which it operated in foreign countries, where the dehydrated milk and milk

[1]The parties also refer to this corporation as International.

products were converted into liquid milk, chocolate drinks, ice cream, and similar products. Since it began business, 95 per cent of Supply's gross income has been derived from sources other than sources within the United States. In 1952, Supply was a party to a contract with the United States which had been executed in 1948 and which was a continuing contract in good standing. Supply also had a contract with the United States to furnish milk products to the Armed Forces in the Far East Command.

In 1952, there was only one class of stock of Supply issued, namely, voting capital stock. There were 5,000 shares outstanding, all of which were owned by Grover D. Turnbow.

In 1952, International Dairy Engineering Co. (hereinafter called Engineering) was engaged in constructing a plant at Atwater, California. Its total outstanding stock consisted of 100 shares, which were owned by Turnbow.

In 1952, the outstanding capital stock of Diamond Dairy, Inc. (hereinafter called Diamond), consisted of 25,000 shares, of which Supply owned 15,000 shares, 60 per cent, and individuals owned 10,000 shares, 40 per cent.

[R. 32] In 1951, Foremost and Turnbow began negotiations and entered into an agreement under which Foremost was to acquire all of the stock of the three corporations above named in what was intended to be a tax-free reorganization. Upon completion of preliminary matters in the early part of 1952, a supplemental agreement, called Amendatory Agreement, was executed by Foremost and Turnbow on February 11, 1952. The amendatory agreement is incorporated herein by this reference. It included, *inter alia*, the reorganization plan.

Under the reorganization plan the following was to be done: (1) Foremost was to acquire from Turnbow all of the capital stock of Supply (5,000 shares), and Turnbow was to receive in exchange 82,375 shares of the common stock of Foremost, plus $3,000,000. Supply was thereby to become a wholly owned subsidiary of Foremost; it was to continue in the operation of its business. (2) Foremost was to acquire from Turnbow all of the outstanding capital stock of International Dairy Engineering Co. (100 shares), and Turnbow was to receive in exchange 60,000 shares of the common stock of Foremost. International Engineering was thereby to become a wholly owned subsidiary of Foremost, and it was to continue in the operation of its business. (3) Under the first exchange of stock, Foremost would gain control of 60 per cent of the capital stock of Diamond Dairy, Inc., which was owned by Supply. Having acquired control of Diamond, Foremost, pursuant to the plan of reorganization, was to acquire the minority stock of [R. 33] Diamond, 10,000 shares, by giving 10,000 shares of Foremost common stock in exchange for 10,000 shares of capital stock of Diamond, which Turnbow agreed to deliver. Neither Supply, Engineering, Diamond, nor Foremost was to make any distribution to its respective shareholders in pursuance of the plan of reorganization, or otherwise.

It was contemplated, under the reorganization plan, that the number of directors of Supply and Engineering would be changed so that Turnbow would maintain three directors thereon and Foremost would elect three Directors; that Supply would create an executive committee consisting of three members, two of which would be nominated

by Foremost; that Turnbow would be the president and general manager of Supply and of Engineering, and that Turnbow's nominee would be president and/or general manager of Diamond; that Turnbow's salary would be in the same amount as the salary of the president of Foremost; that the president of Foremost might become the vice president of Supply and of Engineering, and the chairman of the executive committee of each company; that Turnbow would become a member of the board of directors and of the executive committee of Foremost, and would have the right to nominate two directors, in addition to himself, to Foremost's board of directors; that Turnbow would be elected chairman of Foremost's executive committee; and that Turnbow would execute a formal agreement with Foremost not to compete with either Supply, Engineering, or Foremost in the type of business [R. 34] carried on by each, other than the business of farming, cattle raising, or the farm production of milk. Furthermore, it was contemplated by the parties that there would be two divisions of the business of Foremost, the Eastern division, and the Western and International division; and that Turnbow would be known as the general manager of the Western and International division, and Paul E. Reinhold (the president of Foremost) would be known as the general manager of the Eastern division.

The closing date under the 1952 agreement was March 3, 1952. Prior to the closing date Turnbow was to do the following things: He was to purchase a ranch and certain personal property for cash from Engineering, and he was to convey all title to a patent application to Engineering. Also, he was to pay $500,000 to Engineering

as a capital contribution, and it was agreed that the plant which Engineering was constructing at Atwater would cost in excess of $600,000, and would be completed, substantially, by April 15, 1952. Turnbow was, further, to purchase for cash from Supply certain notes receivable of three stockholders of Diamond for $61,142, and a note of a Dr. Kempf for $3,150.

The terms of the agreement of February 11, 1952, were carried out.

On March 3, 1952, the exchange of the stock of Supply for stock of Foremost was consummated, and Turnbow received 82,375 shares of the common stock of Foremost (a minority interest) in exchange for all of the capital stock of Supply. Turnbow [R. 35] also received cash from Foremost in the amount of $3,000,000. Since his expenses in connection with the exchange were $15,007.23, the net amount of the cash he received was $2,984,992.77.

On March 3, 1952, the 82,375 shares of common stock of Foremost had a fair market value of $15 per share.

In the exchange of the stock of Supply, Foremost acquired all of the issued and outstanding shares of stock of Supply, of all classes. In the exchange, petitioner acquired only the 82,375 shares of common stock of Foremost and cash in the amount of $3,000,000 ("boot"), and Foremost acquired only all of the issued and outstanding shares of the voting capital stock of Supply.

In the income tax return of the petitioner for 1952, he reported long-term capital gain from the above-described transaction in the amount of $2,984,992.77, under the provision of sections 112(b)(3) and 112(c)(1).

The Commissioner's determination was as follows:

In 1952 you exchanged 5,000 shares of International Dairy Supply Company capital stock for $3,000,000.00 in cash and 82,375 shares of capital stock of Foremost Dairies, Inc. You determined that the gain to be recognized was limited to the amount of cash received. In your return you reported a gain of $2,984,992.77 ($3,000,000.00 less $15,007.23 expense of exchange). It is held that the entire gain realized upon the exchange constituted [R. 36] taxable income. The adjustment to the income reported in your return is computed as follows:

Amount received on exchange:		
Cash		$3,000,000.00
82,375 shares of Foremost Dairies, Inc. valued at $15.00 a share		1,235,625.00
Total received		$4,235,625.00
Less: Basis of stock exchanged	$50,000.00	
Expenses per return	20,981.80	
Add'l. legal fees allowed	951.26	
		71,933.06
Gain recognized		$4,163,691.94
Gain reported		2,984,992.77
Additional gain recognized		$1,178,699.17
Adjustment to income—50 per cent		$589,349.59

OPINION.

HARRON, *Judge:* Petitioner owned all of the outstanding stock of Supply, which was voting stock. In 1952, he received in exchange for all of his stock in Supply 82,375 shares of common stock of Foremost and $3,000,000 in cash, so-called "boot." The question before us is limited to whether the provisions of section 112(c)(1) of the 1939 Code[2] [R. 37] apply to the transaction. Respondent has determined that section 112(c)(1) does not apply, and that therefore, the entire gain is taxable under section 112(a).

Petitioner contends that, in considering whether section 112(c)(1) applies to the transaction, it is necessary and proper to look to section 112(b)(3)[3] *after omitting* the cash payment involved in the transaction. Respondent contends that there must be a qualifying reorganization within

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[2]SEC. 112(c). GAIN FROM EXCHANGES NOT SOLELY IN KIND.—

(1) If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5), or within the provisions of subsection (l) of this section if it were not for the fact that, the property received in exchange consists not only of property permitted by such paragraph or by subsection (l) to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

[3]SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) GENERAL RULE.—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(b) EXCHANGES SOLELY IN KIND.—

* * * * * * *

(3) STOCK FOR STOCK ON REORGANIZATION.—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

the meaning of section 112(g)(1)(B)[4] before section 112(c)(1) can come into play insofar as section 112(c)(1) refers to an exchange within the provisions of section 112(b)(3).

[R. 38] Subsection (b) of section 112 allows various exceptions from subsection (a), which states the general rule that the entire amount of the gain shall be recognized upon the sale or exchange of property. Subsection (b) deals with exchanges solely in kind, whereas subsection (c) deals with the treatment of gain from exchanges which are not solely in kind, but only *if* an exchange *would be within* (1), (2), (3), or (5), *if it were not for the fact that the property received in exchange consists* not only of property permitted by (1), or (2), or (3), or (5), but *also of other property or money.* Directing our attention to section 112(b)(3), it is noted that among the requirements contained therein is the specification that the property involved must be stock or securities which is exchanged *solely* for stock or securities. Both of the sections involved here, subsection (b)(3) and subsection (c)(1), are provisions of long standing which were reenacted in the successive revenue acts which preceded the 1939 Code. In both the regulations of the Commissioner and in this Court's interpretation of section 112(c)(1), it has been understood that in order to give effect to the provisions of section 112(c)(1) the *method* to be followed is first to

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[4]SEC. 112(g) DEFINITION OF REORGANIZATION.—As used in this section • • •—

(1) The term "reorganization" means • • •, or (B) the acquisition by one corporation, in exchange solely for all or a part of its voting stock, of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation, • • •

omit the item of cash (or other property) from the transaction and then to determine whether the exchange *would be* within subsection (b)(3). Otherwise, section 112(c)(1) would have no meaning in the context of its references to particular subsections of section 112(b).

[R. 39] In *Luther Bonham,* 33 B.T.A. 1100, 1103-1104 (1936), this Court concluded that the method of applying the statute was as follows:

"It is necessary therefore to determine whether or not the exchange of • • • stock for • • • stock *would be* within the provisions of subsection (b)(3) *if the item of cash had been omitted* and only • • • stock had been received in exchange for • • • stock." [Italics supplied.]

In *Howard v. Commissioner,* 238 F. 2d 943, 948 (1956), reversing 24 T.C. 792, on the basis of a question which was not reached by this Court, the following was stated:

"Thus we may conclude that, in determining when these so-called 'boot' provisions apply, Congress intended that the transaction is to be considered separately and apart from the 'boot' received in determining whether it meets the nonrecognition provisions. If the transaction, absent the 'other property or money,' fulfills the requirements of section 112(b)(3), then gain is to be recognized to the extent that 'boot' is received.

In the instant case, *but for* the cash received in exchange for • • • common stock of Binkley, the transaction would have met the 'solely' requirement of section 112(g)(1)(B) and fallen within the scope of section 112(b)(3). To the extent that 'boot' was received, gain would be recognized under our interpretation of section 112(c)(1). • • •"

The view expressed in *Howard v. Commissioner, supra,* corresponds with the opinion which was expressed by this Court in the *Bonham* case. Our [R. 40] problem here is whether we should adhere to our understanding of the *method* to be followed in determining whether section 112(c)(1) applies in the exchange of stock solely for stock, plus money.

Consideration has been given to the respondent's regulation, Regs. 118, sec. 39.112(g)–4 (issued September 26, 1953, and applicable to taxable years beginning after December 31, 1951), which is set forth in the margin.[5] Regs. 111, sec. 29.112(g)-4 [R. 41] (issued by respondent in October 1943 and applicable to taxable years beginning after December 31, 1941), contain provisions which are identical with Regs. 118, sec. 39.112(g)-4. The provisions of section

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[5]Sec. 39.112(g)-4 *Exchanges in reorganization for stock or securities and other property or money.* (a) If in an exchange of stock or securities in a corporation a party to a reorganization, in pursuance of the plan of reorganization, for stock or securities in the same corporation or in another corporation a party to the reorganization, there is received by the taxpayer other property (not permitted to be received without the recognition of gain) or money, then

(1) As provided in section 112(c)(1), the gain, if any, to the taxpayer will be recognized in an amount not in excess of the sum of money and the fair market value of the other property, but

(2) The loss, if any, to the taxpayer from such an exchange is not to be recognized to any extent (see section 112(c)).

(b) The application of paragraph (a) of this section may be illustrated by the following example:

Example. A, in connection with a reorganization, in 1952, exchanges a share of stock in the X Corporation purchased in 1929 at a cost of $100 for a share of stock of the Y Corporation (a party to the reorganization), which has a fair market value of $90, plus $20 in cash. The gain from the transaction is $10 and is recognized and taxed as a gain from the exchange of property. But see section 117. However, if the share of stock received had a fair market value of $70, the loss from the transaction of $10 would not be recognized.

112(c)(1) of the 1939 Code were reenacted in substantially identical language in section 351(b) of the 1954 Code, and respondent's regulations promulgated under the 1954 Code, section 1.351-2(a) restate in substantially identical language what was stated in Regs. 111, sec. 29.112(g)-4, and Regs. 118, sec. 39.112(g)-4.

Thus, there has been a long-standing and continuous construction of section 112(c)(1) (and the corresponding section in the earlier revenue acts) which has remained unchanged over the years in the face of the several reenactments of the statutory provision, as well as the amendment in the 1934 Act of section 112(g)(1)(B), when there was introduced into subsection (g)(1)(B) the word "solely," in harmony with the provisions of subsections (b)(2), (b)(3), (b)(4), and (b)(5) which also contained the word "solely," and contained "solely" for many years. The respondent's regulations, therefore, are deemed to have received the approval of Congress. *Helvering v. Winmill*, 305 U.S. 79; *Lykes v. United States*, 343 U.S. 118. Respondent has not offered any explanation for his departure in this case from his long-standing interpretation of section 112(c)(1) set forth in his regulations.

In this circumstance, and since this Court's view of the *method* to be followed in applying the pro-[R. 42] visions of section 112(c)(1) is in accord with the respondent's longstanding regulations, we do not find cause for changing our construction of section 112(c)(1), and in this case we conclude that it should be followed.

The respondent's error is that he has seen fit here not to omit the item of cash in determining whether the transaction of petitioner and Foremost involved an exchange

of the stock of Supply solely for stock of Foremost within the provisions of section 112(b)(3).

Accordingly it is held, that *but for* the cash received by petitioner in the transaction involving the exchange of all of the stock of Supply for part of the stock of Foremost, the exchange would have met the "solely" requirement of section 112(g)(1)(B) and fallen within section 112(b)(3). *Howard v. Commissioner, supra* at 948. Therefore, under section 112(c)(1) the gain to petitioner may not be recognized in an amount in excess of $2,984,992.77, which is the net amount of $3,000,000 less allowable expenses.

Recomputations are required under Rule 50 because of concessions or abandonment of the parties in respect to other adjustments.

Decision will be entered under Rule 50.

[R. 43] Tax Court of the United States
Washington

Docket No. 69,429

GROVER D. TURNBOW and RUTH H. TURNBOW,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the determinations of the Court, as set forth in its Findings of Fact and Opinion filed June 12, 1959, the respondent has filed recomputations under Rule 50, with which the petitioners agree. Accordingly, it is

Ordered and Decided: That there are deficiencies in income taxes for the taxable years 1952 and 1953 in the amounts of $5,694.30 and $13,404.73, respectively.

[Seal] Marion J. Harron,
Judge.

Entered August 31, 1959. Served September 1, 1959.

[R. 56] United States Court of Appeals
for the Ninth Circuit

COMMISSIONER OF INTERNAL REVENUE,
Petitioner,

vs.

GROVER D. TURNBOW and RUTH H. TURNBOW,
Respondents.

No. 16,775
Dec. 5, 1960

Upon Petition to Review a Decision of The
Tax Court of the United States

Before: MERRILL and KOELSCH, Circuit Judges, and BOWEN, District Judge.

MERRILL, Circuit Judge:

This case presents the following question: whether gain realized by a taxpayer upon the transfer of his stock in a wholly owned corporation in consideration for voting stock in another corporation plus cash is recognizable in its entirety or only to the extent of the cash received. The Tax Court, following Howard vs. Commissioner of Internal Revenue, 7 Cir., 1956, 238 F.2d 943, has ruled that the gain is recognizable only to the extent of the cash received. Grover D. Turnbow, 32 T.C. 646. We have concluded that this was error and that the gain is recognizable in its entirety.

The taxpayer, Turnbow, was the sole stockholder of International Dairy Supply Company, a Nevada corporation which had its principal place of business in San Fran-

cisco, California. In 1952, the taxpayer transferred his stock in that company to Foremost Dairies, Inc., a New York corporation which had its principal place of business in Jacksonville, Florida. This transfer was in exchange for 82,375 shares of the common stock of Fore-[R. 57]most and $3,000,000.00 cash, so-called "boot." The Foremost shares were of a value of $1,235,625.00. Thus the shares constituted 29% of the total consideration received, while the boot constituted 71%.

The taxpayer reported a capital gain on the transaction limited to the $3,000,000.00 cash boot, less expenses which by agreement he had undertaken to assume. The Commissioner determined that the entire gain on the transaction was taxable, establishing that gain at $4,163,691.94. Tax deficiencies for the years 1952 and 1953 in the amounts, respectively, of $264,037.43 and $14,786.26 were determined.

The taxpayer petitioned the Tax Court for review. That court held that gain on the transaction should be limited to the cash boot. The deficiencies were disallowed. The Commissioner has petitioned this court for review.

The problem presented involves construction of § 112 of the Internal Revenue Code of 1939, which deals with recognition of gain or loss.

Section 112(a) sets forth the general rule that "upon the sale or exchange of property the entire amount of gain or loss * * * shall be recognized, except as hereinafter provided in this section."

Among the exceptions specified, § 112(b) deals with exchanges solely in kind, and § 112(b)(3) deals with ex-

changes of stock for stock on reorganization. It provides:

> "No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization."

The term "reorganization," as used in § 112(b)(3), is defined in § 112(g)(1), which, as amended in 1943, provides:

> "The term 'reorganization' means (A) a statutory merger or consolidation, or (B) the acquisition by one corporation, in exchange solely for all or a part of its voting stock, of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation, or (C) the acquisition by one corporation, in exchange solely for all or a part of its voting [R. 58] stock, or substantially all the properties of another corporation, but in determining whether the exchange is solely for voting stock the assumption by the acquiring corporation or a liability of the other, or the fact that property acquired is subject to a liability, shall be disregarded, or (D) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its shareholders or both are in control of the corporation to which the assets are transferred, or (E) a recapitalization, or (F) a mere change in identity, form, or place of organization, however, effected."

In this case we are concerned with the definition set forth in Clause (B) of § 112(g)(1). Our discussion also deals with the definition set forth in Clause (C). Today

these types of reorganization are known to the tax bar as (B) and (C) reorganizations and we shall take advantage of this terminology.

Section 112(c) is the section upon which the taxpayer relies for his right to limit recognition of gain to the cash boot. As amended in 1943, § 112(c)(1) provides:

> "If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5), or within the provisions of subsection (1), of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph or by subsection (1) to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property."

The dispute before us is as to the method to be followed in applying § 112(c) to the facts of a case. The Tax Court purported to follow its earlier decision upon this problem in Luther Bonham, 1936, 33 B.T.A. 1100, 1103-1104. It quoted that opinion (supplying its own emphasis) as follows:

> "It is necessary therefore to determine whether or not the exchange of * * * stock for * * * stock *would be* within the provisions of subsection (b)(3) *if the item of cash had been* [R. 59] *omitted* and only * * * stock had been received in exchange for * * * stock."

Howard vs. Commissioner of Internal Revenue, supra at page 948, was also quoted to the following effect:

> "In the instant case, *but for* the cash received in exchange for * * * common stock of Binkley, the trans-

> action would have met the 'solely' requirement of section 112(g)(1)(B) and fallen within the scope of section 112(b)(3). To the extent that 'boot' was received, gain would be recognized under our interpretation of section 112(c)(1)."

Applying this method to the case at bar, the taxpayer reasons: but for the cash received, the transaction—solely stock for stock—would have met the "solely" requirements of both §§ 112(b)(3) and 112(g)(1)(B) and fallen within the nonrecognition provision of § 112(b)(3). Therefore, he says, under § 112(c) the gain to be recognized is limited to the amount of the cash received.

The Commissioner contends that § 112(b)(3) requires an actual and not a hypothetical reorganization before nonrecognition can result; that petitioner's method assumes the absence of boot not only to determine whether § 112(b)(3) would apply but also to determine whether the §112(g)(1)(B) definition would apply; that this does violence to § 112(b)(3), which expressly contemplates the existence of a reorganization.

The method of applying § 112(c), advocated by the Commissioner, is to ascertain first whether a reorganization exists under § 112(g)(1). If it does, then and only then can the nonrecognition provisions of § 112(b)(3) become applicable. If it does not, § 112(b)(3) cannot apply. Only when § 112(b)(3) applies, can § 112(c) operate to modify its consequences.

Applying this method to the case at bar, the Commissioner reasons that, since the presence of boot precludes a (B) reorganization, § 112(b)(3) cannot apply and the gain is subject to taxation under § 112(a). Under the Com-

missioner's construction, (B) and (C) reorganizations are forever excluded from the operation of § 112(c). The other types of reorganizations specified in § 112(g)(1), however, do remain subject to the operation of § 112(c).

[R. 60] Upon this dispute, legislative history supports the Commissioner's position.

Prior to 1934, there were no (B) or (C) reorganizations as such.[1] Section 112(i) of the Revenue Act of 1932 (the prior analogous section to § 112(g)(1) of the 1934 Act) read in pertinent part:

> "The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation)."

The provisions of §§ 112(b)(3) and 112(c), however, existed in substantially their present form.

The reasons for the 1934 amendment of § 112(g)(1) are clearly disclosed by congressional reports and discussion. The House Ways and Means Committee Report, H. Rep. No. 704, 73d Congress, 2d Session 13 (1934) states:

> "The reorganization provisions have been in effect for many years, having been adopted in substantially their present form in 1924. They state in detail how each step of a reorganization should be treated for tax purposes. The policy was adopted of permitting reorganizations to take a wide variety of forms, with-

[1] Even the 1934 amendment did not separate (B) and (C) reorganizations. Both were dealt with under Clause (B). It was not until the Internal Revenue Code of 1939 that the separation occurred which has given rise to today's terminology.

out income-tax liability. As a result, astute lawyers frequently attempted, especially during the prosperous years, to take advantage of these provisions by arranging in the technical form of a reorganization, within the statutory definition, what were really sales."

A letter from the Secretary of the Treasury, which appears in the Congressional Record, 78 Cong. Rec. 2512 (1934) states:

"Exchanges and reorganizations. The Treasury regards it as desirable that business readjustments be permitted without tax consequences in cases where the stockholders in the enter-[R. 61]prise are retaining their interests without the receipt of cash and the essential continuity of the business is being preserved. On the other hand, the Treasury has suffered a considerable loss of revenue in recent years through the adroitness of attorneys in planning sales in such a way as to come within the scope of the reorganization provisions. The bill revises the definition of reorganization in order to eliminate serious loopholes in this provision, while legitimate exchanges and reorganizations may still be carried out without the realization of gain or loss. In the opinion of the Department, a considerable saving in revenue will result from these amendments without the injurious effects to business which would have been caused by a complete elimination of these provisions."

A subcommittee of the House Ways and Means Committee, studying the revision of the revenue act, was sufficiently exercised over avoidance practices to give serious consideration to the advisability of eliminating completely the provisions governing reorganization exchanges. H. Rep., December 4, 1933, 73d Congress, 2d Session, 8-9

(1933). However, the House Ways and Means Committee, in its report, stated:

> "The committee decided that, under present conditions, the wiser policy is to amend the provisions drastically to stop the known cases of tax avoidance, rather than to eliminate the sections completely." H. Rep. No. 704, 73d Congress, 2d Session, 13 (1934).

The House committee's solution was to eliminate from the definition of reorganization, as it then appeared in Clause (A), the parenthetical phrase following the words "merger or consolidation."

Had this solution been adopted, there would have been no (B) or (C) reorganizations and § 112(c) obviously could have no reference to such transactions.

The Senate Finance Committee reported, S.Rep. No.558, 73d Congress, 2d Session, 16 (1934):

> "Your committee is in complete agreement with the purposes of the House bill which aim at tax avoidance schemes in [R. 62] this connection. However, some modifications are recommended in order to bring about a more uniform application of the provisions in all 48 of the States. Not all of the States have adopted statutes providing for mergers or consolidations; and, moreover, a corporation of one State cannot ordinarily merge with a corporation of another State. The committee believes that it is desirable to permit reorganizations in such cases, with restrictions designed to prevent tax avoidance. Consequently, the committee recommends the insertion in the House bill of an addition to the definition of the term 'reorganization' as follows: * * *"

Then follows the Clause (B) definition which was eventually incorporated into § 112(g)(1) of the 1934 act.

Emphasizing its views that the tax avoidance problems would be met, the report states at page 17:

> "It will be noted that the proposed amendment requires that * * * the acquisition, whether of stock or of substantially all the properties, must be in exchange solely for the voting stock of the acquiring corporation."

It is clear from this history that, with specific abuses in mind, Congress sought to eliminate them by requiring that, for an acquisition to qualify for the tax advantages of a reorganization, it must be in exchange solely for voting stock.

With reference to this requirement the Supreme Court has stated in Helvering vs. Southwest Consolidated Corporation, 1941, 315 U.S. 194, 198:

> "But clause B of § 112(g)(1) of the 1934 Act effects an important change as respects transactions whereby one corporation acquires substantially all of the assets of another. See S. Rep. No. 558, 73d Cong., 2d Sess., Committee Reports, Revenue Acts 1913-1938, pp. 598-599. The continuity of interest test is made much stricter. See Paul, Studies in Federal Taxation (3d Series), pp. 36-41. Congress has provided that the assets of the transferor corporation must be acquired in exchange 'solely' for 'voting stock' of the transferee. 'Solely' leaves no leeway. Voting stock plus some other consideration does not meet the statutory requirement. See [R. 63] Hendricks, Developments in the Taxation of Reorganizations, 34 Col. L. Rev. 1198, 1202-1203."

Certainly it could not have been intended by Congress that this result would be frustrated at birth by the already existing provisions of § 112(c); yet such would seem to be the effect of the taxpayer's construction.

The Commissioner's construction seems supported by subsequent congressional action. If (B) reorganizations can hypothetically exist notwithstanding boot, the same would apply to today's (C)-type reorganizations, which also were created by the 1934 amendments.

> "* * * the acquisition by one corporation, in exchange solely for all or a part of its voting stock; * * * of substantially all the properties of another corporation * * *." § 112(g) (1) (B) of the Revenue Act of 1934.

Yet, in 1939, Congress saw fit to amend the definition of (C) reorganizations by providing:

> "* * * but in determining whether the exchange is solely for voting stock the assumption by the acquiring corporation of a liability of the other, or the fact that property acquired is subject to a liability, shall be disregarded * * *." § 112(g) (1) (C) of the Internal Revenue Code of 1939.

In § 368(a) (2) (B) of the Internal Revenue Code of 1954, the definition was further amended to provide that only 80% of the assets of the acquired corporation need be obtained in exchange for voting stock; that boot could, without defeating reorganization, be the consideration for assets above 80%. Under the taxpayer's construction, neither of these amendments was necessary. That Congress felt it necessary so to amend the section indicates that the Commissioner's construction reflects the true congressional intent and understanding.

The taxpayer refers us to a point emphasized in Howard vs. Commissioner of Internal Revenue, supra. Section 112(e) is the counterpart of § 112(c), the latter dealing with recognition of gains and the former with recognition

of losses. Section 112(e) [R. 64] has remained virtually unchanged since its original enactment as § 203(f) of the Revenue Act of 1924. It provides:

> "If an exchange would be within the provisions of subsection (b) (1) to (5), inclusive, or (10), or within the provisions of subsection (l), of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain or loss, but also of other property or money, then no loss from the exchange shall be recognized."

Howard points out that if the presence of boot results in recognition of gains it likewise results in recognition of losses; that a taxpayer desiring that a loss be recognized might convert what otherwise would be a legitimate reorganization into a sale by the payment of a trifling amount of cash; that such a construction would thus defeat the 1924 legislative intent in enacting § 112(e).

It would appear, however, that Congress in 1934 was aware that attempts might be made under the proposed amendment to secure recognition of losses notwithstanding actual continuity of interest. The House Ways and Means Committee, as we have noted, recommended that the "acquisition" type of transaction (the forerunner of today's (B) and (C) reorganizations) be completely eliminated from the definition of reorganization. At the same time the report stated:

> "Furthermore, the retention of the other reorganization provisions will prevent large losses from being established by bondholders and stockholders who receive securities in a newly reorganized enterprise which are substantially the same as their original in-

vestments." H. Rep. No. 704, 73d Congress, 2d Session, 14 (1934).

Thus it would appear that in the judgment of Congress the danger of tax avoidance (through securing recognition of losses notwithstanding continuity of interest) was avoided by the probability that the acquisitions resulting in loss could be treated as reorganizations under the remaining provisions of § 112(g) (1).[2]

[R. 65] Whether this judgment was sound apparently still remains to be tested. However, Congress would seem to have weighed the desirable features of the proposed amendment (as to gains) against its undesirable potentialities (as to losses). For us to permit the possibility of tax avoidance under § 112(e), to control our construction of § 112(c), would be to overrule the apparent judgment of Congress upon this very question.

The Tax Court opinion in this case points out that the Commissioner's regulations are deemed to have received

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[2]The judgment of Congress would also seem to have taken into consideration the apparent lack of effectiveness of § 112(e) in preventing loss taking in corporation exchange transactions. The report of the subcommittee of the House Ways and Means Committee stated in H. Rep., December 4, 1933, 73d Congress, 2d Session 37-42 (1933):

> "The statute provides that upon sale or exchange of property the entire amount of gain or loss shall be recognized with certain exceptions. The exceptions are the exchange and reorganization provisions already referred to. If a taxpayer desires to take a loss, it is easy to arrange a transaction falling without the exceptions. On the other hand, if it is desired to pay no tax on the gain, the transaction can be so arranged as to come within the exception. In addition, losses from the sale or exchange of stocks and bonds are limited, to a large extent, to gains from such sales or exchanges so in many cases a stock or bond loss, even if recognized, could not be utilized by the taxpayer."

This quote also appears at: Hearings before the House Committee on Ways and Means on the 1934 Revenue Bill, 73d Congress, 2d Session 60 (1934).

the approval of Congress (citing Lykes vs. United States, 1951, 343 U.S. 118; Helvering vs. Winmill, 1938, 305 U.S. 79) and places reliance upon the Commissioner's regulations, 118, § 39.112(g)-4. In our view, this section casts little light on the problem. On the other hand, § 39.112(g)-1 (c) of the regulations lends support to the Commissioner's position. It provides in part:

> "From its context the term 'a party to a reorganization' can only mean a party to a transaction specifically defined as a reorganization by section 112(g). • • • The provisions of the Internal Revenue Code referred to in this paragraph [this includes § 112(c)] are inapplicable unless there is a plan of reorganization. A plan of reorganization must contemplate the bona fide execution of one of the transactions specifically described as a reorganization in section 112(g) [R. 66] and for the bona fide consummation of each of the requisite acts under which nonrecognition of gain is claimed."

We conclude that, if the "solely for voting stock" requirement of (B) and (C) reorganizations is to be given the effect intended by Congress, § 112(c) cannot operate to render a stock-plus-boot acquisition a (B) or (C) reorganization through a disregard of the existence of boot. In the case before us, then, the existence of boot prevents § 112(g) (1) (B) from applying; since no reorganization exists, § 112(b) (3) cannot apply; § 112(c) is then also inapplicable.

Reversed and remanded with instructions that the deficiencies determined by the Commissioner be reexamined in the light of this opinion.

(Endorsed) Opinion Filed Dec. 5, 1960.

Frank H. Schmid, Clerk.